

Message Text

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ACTION NEA-10

INFO OCT-01 EUR-12 ISO-00 IO-13 SSM-03 SP-02 USIA-06
AID-05 EB-08 NSC-05 TRSE-00 SS-15 STR-07 OMB-01
CEA-01 CIAE-00 COME-00 FRB-03 INR-10 NSAE-00
XMB-02 OPIC-03 LAB-04 SIL-01 AGRE-00 DOE-15 SOE-02
HA-05 /134 W

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R 310905Z MAR 78
FM AMEMBASSY BEIRUT
TO SECSTATE WASHDC 7373
INFO AMEMBASSY AMMAN
AMEMBASSY ATHENS
AMEMBASSY CAIRO
AMEMBASSY DAMASCUS
AMEMBASSY PARIS
AMEMBASSY TEL AVIV

C O N F I D E N T I A L SECTION 1 OF 2 BEIRUT 1769

ATHENS FOR RTDO

E.O. 11652: GDS
TAGS: EGEN, EFIN, LE
SUBJECT: LEBANESE ECONOMIC CLIMATE: FIRST QUARTER 1978

REF: (A) 77 BEIRUT 6469, (B) STATE A-0463 (CERP 003)

1. SUMMARY: ECONOMIC ACTIVITY AND BUSINESS CONFIDENCE
IN LEBANON REACHED A POST-WAR PEAK IN EARLY FEBRUARY,
THEN TURNED DOWN IN RESPONSE TO DETERIORATING SECURITY
CONDITIONS. THE ISRAELI INVASION MARCH 15 ALL BUT
ECLIPSED THE FEW BRIGHT SPOTS OF THE QUARTER, AND THE
PERIOD CLOSED IN A MODD OF ANXIETY. THE OUTLOOK FOR THE
SECOND QUARTER IS MILDLY PESSIMISTIC. END SUMMARY.

2. FIFTEEN MONTHS AFTER THE END OF CIVIL HOSTILITIES,
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LEBANON REMAINS A COUNTRY WITHOUT MOST KEY STATISTICS
AND STILL BEGINNING TO SORT ITSELF OUT ECONOMICALLY.
THE GOVERNMENT STUDIES, DEBATES AND PROMISES. MAJOR
ENTREPRENEURS WATCH, AND IN THE FIRST QUARTER OF 1978,
ARE STILL WAITING FOR EVIDENCE OF PUBLIC SECURITY
SUFFICIENT TO JUSTIFY LARGE INVESTMENTS. SMALLER
ENTREPRENEURS ARE THE DOERS AND BUILDERS; THEY, NOT

THE GOL, LEAD WHAT REVIVAL ONE SEES. MEANWHILE, LEBANON'S POST-WAR ECONOMY IS HEAVILY SUPPORTED BY THE REMITTANCES OF SKILLED REFUGEES ABROAD. CAPITAL FLIGHT EXCEEDED DOMESTIC INVESTMENT BY ROUGHLY TWO TO ONE DURING 1977, YET DOMESTIC LIQUIDITY CONTINUES TO GROW OWING TO THE RELUCTANCE OF INVESTORS TO COMMIT FUNDS.

3. OVERALL ECONOMIC TREND: THE ECONOMIC UPSWING DESCRIBED IN THE POST'S YEAR-END REPORT (REFTEL), CONTINUED IN JANUARY, MARKED BY BROADENING RECOVERY ON THE RETAIL LEVEL AND MODEST BUT GROWING INDUSTRIAL REINVESTMENT WITH THE HELP OF BANK CREDIT. BUSINESS CONFIDENCE INCREASED. A REVERSAL OCCURRED FEBRUARY 7 WHEN THE FAYYADIYEH OUTBREAK FOLLOWED BY TWO WEEKS OF STREET CONFLICT IN CHRISTIAN AREAS EXPOSED THE WEAKNESS OF LEBANON'S INTERNAL SECURITY ARRANGEMENTS. THE MONTH ENDED IN AN ATMOSPHERE OF TENSION. THE ISRAELI INCURSION MARCH 15 THEN RAISED INCALCULABLE NEW DOUBTS. WHEREAS FAYYADIYEH CHECKED THE TEN-MONTH EXPANSIONARY TREND THAT HAD MARKED LEBANON'S ECONOMY SINCE KAMAL JUNBLATT'S MURDER IN MARCH 1977, THE ISRAELI INCURSION DEALT A SEVERE BLOW TO BUSINESS OPTIMISM. UNCERTAINTY WILL DOMINATE THE SECOND QUARTER OF 1978 AS BUSINESSMEN ADJUST TO THE NEW SITUATION.

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4. ECONOMIC INDICATORS: NATIONAL INCOME AND BALANCE OF PAYMENTS STATISTICS HAVE NOT APPEARED SINCE 1974. BANKS, WTDR INTERVIEWS, AND BUSINESS SOURCES PROVIDED THE FOLLOWING IMPRESSIONISTIC VIEW.

-- INDUSTRY: OUTPUT AND REINVESTMENT EXPANDED EARLY IN THE QUARTER. CEMENT PRODUCERS OPERATED AT ABOUT 85 PERCENT OF AVAILABLE CAPACITY AND IMPORTED EXTRA PRODUCT TO MEET DEMAND. THE TWO REFINERIES OPERATED AT AN AVERAGE 34,000 BBL/DAY, 70 PERCENT OF CAPACITY, OWING TO A MAINTENANCE SHUTDOWN OF THE TRIPOLI REFINERY IN FEBRUARY. BANK LENDING TO INDUSTRIAL BORROWERS INCREASED, BUT LOANS WERE FOR REPAIR AND EXPANSION OF EXISTING PLANT RATHER THAN FOR NEW ENTERPRISES. ELECTRICITY CONSUMPTION EXCEEDED THE COMPARABLE LEVELS IN 1977 AND 1974, BUT NO BREAKOUT OF INDUSTRIAL USAGE WAS AVAILABLE.

-- CONSTRUCTION: ACTIVITY INCREASED, MOST VISIBLY IN WEST BEIRUT WHICH LAGGED THE EASTERN SECTOR IN 1977. CLEANUP AND RECONSTRUCTION IN THE DESTROYED DOWNTOWN CONTINUED, BUT LESS ENERGETICALLY THAN IN

PERIPHERAL AREAS. NO VISIBLE WORK WAS DONE ON THE MAJOR HOTELS DURING THE QUARTER. ACCORDING TO LOCAL PRESS, A DECISION TAKEN IN LATE 1977 TO REHABILITATE THE PHOENICIA HOTEL, STARTING APRIL 1 WAS PLACED IN ABEYANCE AFTER THE FAYYADIYEH INCIDENT. THE REFUGEE INFLUX FOLLOWING ISRAEL'S INCURSION SERIOUSLY AFFECTED PROPERTY VALUES AND MORTGAGES IN WEST BEIRUT AND, IF THE REFUGEES STAY, WILL DEPRESS CONSTRUCTION IN THE AREA NEXT QUARTER.

-- COMMERCE: PORT AVERAGED 218,500 TONS/MO (AVERAGE JULY-DECEMBER 1977 WAS 216,000 TONS/MO). LAST OF FOUR AID-BUILT WAREHOUSES CAME INTO SERVICE DURING THE QUARTER. AIR TRAFFIC DIPPED SEASONALLY, CONFIDENTIAL

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AVERAGING 102,000 PASSENGERS AND 2225 FLIGHTS/MONTH (AVERAGE JULY - DECEMBER 1977 WAS 133,271 PASSENGERS AND 2262 FLIGHTS/MO). QUARTERLY FIGURES FOR LEBANESE IMPORTS AND EXPORTS WERE UNAVAILABLE, BUT PRELIMINARY EXPORT DATA FOR FEBRUARY SHOW A DECLINE FROM JANUARY TOTALS EXACTLY EQUALING THE DECLINE IN EXPORTS OF CEMENT. CEMENT EXPORTS WERE STIFLED FOR APPROXIMATELY THREE WEEKS BY CLOSURE OF THE DAMASCUS HIGHWAY DURING THE FAYYADIYEH OUTBREAK. SMUGGLING INCREASED DURING THE QUARTER; IT RANKS AS AN IMPORT SUBECONOMY IN ITS OWN RIGHT.

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C O N F I D E N T I A L SECTION 2 OF 2 BEIRUT 1769

5. BANKING AND MONEY: THE SITUATION DESCRIBED IN OUR YEAR-END REPORT CHANGED LITTLE OVER THE QUARTER. WHILE THE GOL DOES NOT DISCUSS THE ROLE OF EMIGRANT REMITTANCES, THE DISPARITY BETWEEN LIQUIDITY IN THE BANKING SYSTEM AND THE REAL VALUE OF GOODS AND SERVICES PRODUCED BY THE ECONOMY INDICATES THAT REMITTANCES ARE ENTERING LEBANON IN LARGE AMOUNTS. PRIVATE BORROWING REMAINED AT DEPPRESSED LEVELS OWING TO THE POLITICAL SITUATION. GOL BORROWINGS FROM THE PRIVATE SECTOR THROUGH TREASURY BILLS CONTINUED SUCCESSFULLY. CENTRAL BANK PURCHASES OF DOLLARS MODERATED THE DOLLARS DECLINE AGAINST THE POUND (LL 3.05/\$1 IN JANUARY, LL 2.92/\$1 MARCH 30). THE POUND SLUMPED ON TWO OCCASIONS AS FAYYADIYEH AND THE ISRAELI INCURSION STRENGTHENED DEMAND FOR FOREIGN CURRENCIES AND STIMULTATED WITHDRAWALS FROM LOCAL SAVINGS ACCOUNTS. THE \$150 MILLION EURODOLLAR LOAN SYNDICATION PROVIDED A BAROMETER OF EXTERNAL CONFIDENCE
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IN LEBANON. SUBSCRIBER INTEREST, REPORTED AT DOUBLE THE FACE AMOUNT IN LATE JANUARY, DECLINED \$75 MILLION AS MANY BANKS CHOSE NOT TO PARTICIPATE IN MARCH.

6. USEFUL GOVERNMENT DECREES: THE GOL ISSUED A SERIES OF DECREES DECEMBER 31, 1977, THE FINAL DAY OF ITS EMERGENCY POWERS. FOUR DECREES EXTENDED THE GOVERNMENT'S BORROWING OR LOAN GUARANTEEING POWERS IN THE FIELD OF NATIONAL RECONSTRUCTION:

-- DECREE 140 GRANTED GOL GUARANTEE TO COUNCIL FOR DEVELOPMENT AND RECONSTRUCTION (CDR) BORROWINGS FROM ARAB FUND FOR SOCIAL AND ECONOMIC DEVELOPMENT (\$39 MILLION FOR ELECTRICITY NETWORK AND POST RECONSTRUCTION), THE ABU DHABI FUND FOR ARAB ECONOMIC DEVELOPMENT (\$155.8 MILLION FOR ELECTRICITY NETWORK AND SPORT RECONSTRUCTION), AND THE KUWAIT FUND FOR ARAB ECONOMIC DEVELOPMENT (\$28.4 MILLION FOR AIRPORT RECONSTRUCTION). THESE LOAN AGREEMENTS WERE ORIGINALLY ANNOUNCED IN 1977 AND HAVE NOT BEEN FULLY DRAWN.

-- DECREE 142 GRANTED GOL GUARANTEE TO CDR FOR

\$150 MILLION EURODOLLAR LOAN FOR UNDESIGNATED RECONSTRUCTION PURPOSES. BANK OF AMERICA LEAD-MANAGED THIS LOAN, THE SUBSCRIPTION DATE FOR WHICH WAS TO HAVE EXPIRED MARCH 23, 1978. THE EVENTS OF FEBRUARY AND MARCH REDUCED SUBSCRIBER INTEREST, LEAVING THE SYNDICATION CO-MANAGERS TO ABSORB \$70 - 80 MILLION ON THEIR OWN ACCOUNTS.

-- DECREE 144 AUTHORIZED THE CDR TO GUARANTEED ON BEHALF OF THE GOL PRIVATE SECTOR LOANS TO WARDAMAGED TOURISTIC, INDUSTRIAL AND HOSPITAL ENTERPRISES UP TO A \$67 MILLION
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(LL200 MILLION) CEILING.

-- DECREE 145 EXTENDED UNTIL DECEMBER 31, 1978, GOL EMERGENCY AUTHORITY TO BORROW FROM THE CENTRAL BANK, NO LIMITATION SPECIFIED.

7. IN ADDITION TO THE ABOVE THE GOL IMPLEMENTED AN EARLIER DECREE-LAW AUTHORIZING THE CDR TO MAKE DIRECT LOANS TOTALING \$100 MILLION (LL300 MILLION) TO WAR DAMAGED TOURISTIC, INDUSTRIAL AND HOSPITAL ENTERPRISES, AND ISSUED DECREES AUTHORIZING FUNDS FOR RECONSTRUCTION OF DAMAGED SCHOOLS, VOCATIONAL TRAINING CENTERS, AND PRIVATE PROPERTY, FOR AIRPORT DEVELOPMENT (\$142 MILLION), AND FOR REPLACEMENT OF BEIRUT'S BUS FLEET. OTHER DECREES EXTENDED THE DEADLINE FOR PAYING BACK-TAXES AND SET THE STAGE FOR RECONSTRUCTION OF DOWNTOWN BEIRUT. MANY OF THESE DECREES STILL LACK IMPLEMENTING DOCUMENTATION. NEVERTHELESS, THEY SIGNAL GOL SUPPORT FOR NATIONAL REHABILITATION.

8. CLIMATE FOR U.S. BUSINESS: THE CLIMATE FOR U.S. BUSINESS IN LEBANON DETERIORATED DURING THE QUARTER. OF GREATEST IMPORTANCE WERE FAYYADIYEH AND THE ISRAELI INCURSION. IN ADDITION, EXTRA-GOVERNMENTAL "TAXATION" OF BUSINESSES, BOTH FOREIGN AND DOMESTIC, BY LOCAL POLITICAL/SECTARIAN FACTIONS INTENSIFIED. ONE U.S. AFFILIATE DECIDED TO TRANSFER PART OF ITS OPERATION FROM EAST TO WEST BEIRUT IN AN EFFORT TO ESCAPE HARRASSMENT BY MARONITE FUND-RAISERS. STREET SECURITY DETERIORATED: BOMBINGS INCREASED IN JANUARY, THE FAYYADIYEH CLASH FORCED SHOPS AND SCHOOLS TO CLOSE IN PARTS OF EAST BEIRUT AREA FOR TWO WEEKS IN FEBRUARY; ARMED IRREGULARS REAPPEARED ON THE STREETS IN MARCH AND BEGINNING MARCH 15 PATROLLED PARTS OF WEST BEIRUT OPENLY AFTER
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DARK. LOOKING TO THE FUTURE, THE EFFECTS OF ISRAEL'S
OCCUPATION OF THE SOUTH ARE STILL UNFOLDING BUT AT
A MINIMUM THEY INCLUDE INCREASED REFUGEE PRESSURE
UPON THE PRODUCTIVE CENTERS NEAR BEIRUT AND A COM-
PRESSION OF THE SOCIETY AS PALESTINIANS MOVE NORTH-
WARD INTO GREATER CONTACT WITH THE LEBANESE COMMUNITY.
THAT CONTACT MAY PROVE EXPLOSIVE.

9. COMMENT: U.S. AS WELL AS LEBANESE BUSINESSMEN
WERE JOLTED BY THE EVENTS OF FEBRUARY. AS MARCH DRAWS
TO A CLOSE, THE PREVAILING BUSINESS SENTIMENT IS
ANXIETY. NO U.S. FIRMS TO OUR KNOWLEDGE ESTABLISHED
AN EXPATRIATE PRESENCE IN BEIRUT DURING THE QUARTER
AND WE KNOW OF TWO, 3M AND HONEYWELL, WHO ARE THINKING
OF LEAVING. UNTIL THINGS CHANGE FOR THE BETTER, THE
RISK TO POTENTIAL U.S. BUSINESS NEWCOMERS TO LEBANON
MUST BE TERMED HIGH. THE FIRMS ALREADY ESTABLISHED
HERE HAVE BATTENED DOWN IN RESPONSE TO THE RISKS AND
LIKE VETERANS ANYWHERE ARE SAYING "IT DOESN'T LOOK
BRIGHT BUT WE'VE SEEN WORSE." OPTIMISM IS THIN AS
BUSINESSES WONDER HOW LEBANON CAN ACCEPT, MUCH LESS
ABSORB, THE PALESTINIANS WHO WERE ALREADY A NATIONAL PROBLEM
SOUTH OF THE LITANI LAST MONTH, IN WHAT NOW SEEM THE
GOOD OLD DAYS.
PARKER

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